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C O N F I D E N T I A L SECTION 01 OF 04 TAIPEI 004063

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SUBJECT: MAC CHAIRMAN PREDICTS CROSS-STRAIT TOURISM
AGREEMENT WILL BE CONCLUDED SOON

REF: A. TAIPEI 3926

[1](#)B. TAIPEI 4029

Classified By: AIT Director Stephen M. Young, Reason 1.4 d

[1](#)1. (C) Summary. MAC Chairman Wu told the Director December 5 that a cross-Straits agreement to further open Taiwan to PRC tourism would likely be concluded shortly after the December 9 Taipei and Kaohsiung mayoral elections. He said charter flights will take longer, though he expects the Ministry of Economic Affairs (MOEA) should be able to approve in late December the long-delayed applications of Promos and Powerchip to build semiconductor factories in China. Taiwan continues to evaluate relaxing technology limits on semiconductor manufacturing investment, and the 40 percent ceiling on investment. However, it appears as if the Taiwan Solidarity Union (TSU) has the final say on how far the Chen Administration is willing to move on cross-Straits economic integration. Wu predicted that Premier Su Tseng-chang was likely to resign if the Democratic

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Progressive Party (DPP) loses both of the mayoral elections. End summary.

Tourism Agreement Soon

[1](#)2. (C) At a December 5, 2006, meeting with AIT Director Young, MAC Chairman Joseph Wu said cross-Straits discussions on tourism were progressing well. Wu explained that the two sides had held successful preliminary negotiations three weeks ago and again on December 3. In the last round, he said, the two sides resolved two important technical issues: PRC tourists would have to enter and leave Taiwan in tour groups and procedures for repatriating tourists who attempt to overstay.

[1](#)3. (C) On the timing of a tourism agreement, Wu told the Director that MAC had hoped to conclude negotiations in October, but the PRC dragged its feet. He expressed hope that the two sides will be able to meet in formal negotiations to conclude the agreement shortly after the

December 9 elections. In contrast to earlier reports (ref A), Wu indicated that the two sides would not wait for an agreement on charter flights before concluding an agreement on tourism. The Director reiterated U.S. support for this type of opening and underscored the benefit to Taiwan of exposing more people in the Mainland to the reality of life in Taiwan.

¶4. (C) Wu was also quick to point out that the tourism negotiations were conducted based upon a modification of the 2005 Macau Model used to negotiate charter flights. Under the Macau Model, negotiations are nominally led by industry associations with government officials imbedded in the two delegations. In the present case, however, Wu said the tourism discussions were conducted by specially-formed organizations, which Taiwan considers to be official in nature even if the PRC views them as private. He emphasized that the organization representing Taiwan (the Taiwan Strait Tourism Association) is headed by the Director General of the Tourism Bureau of the Ministry of Transportation and Communications.

Charter Flights Later

¶5. (C) Wu was less optimistic about progress on cargo and weekend passenger charter flights. He told the Director that the two sides had been in regular contact since June, but there had been no decision on when to convene more formal consultations necessary to conclude a charter flight agreement. As a positive sign, Wu noted that the PRC had expressed to MAC three weeks ago its willingness to discuss routing charter flights through Japanese airspace. This would dramatically shorten the flight time for charter flights from Taiwan to Shanghai and Beijing, which up until now have had to fly through Hong

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Kong airspace. The PRC had previously rejected this Taiwan proposal to prevent any appearance the routes would be international ones. Wu hopes that the PRC will discuss this flight transit issue during negotiations to conclude an agreement on cargo and weekend passenger charters. He commented that the negotiations would have to be finished by July or August when campaigning for Taiwan's Legislative Yuan and Presidential elections would make further progress impossible.

Semiconductor Opening Too

¶6. (C) The Director asked Wu about the applications by ProMOS and Powerchip, two of Taiwan's leading semiconductor manufacturing firms, to build factories in the PRC. The applications were submitted in December 2004, but MOEA has yet to make a decision. Wu indicated that Taiwan was likely to approve the applications in late December. He said Minister of Economic Affairs Steve Chen had informed him that Chen's ministry would schedule a final review on the applications for December ¶18. Explaining that MAC and MOEA discussions with the deep-Green Taiwan Solidarity Union (TSU) about the applications had gone fairly well, Wu predicted the TSU would not attempt to block the applications again and that they would be approved after the final MOEA review.

¶7. (C) Wu also told the Director that MOEA was working on further relaxation of technology restrictions for semiconductor manufacturing investment in the Mainland. Taiwan currently permits investment in factories capable of producing chips with feature size no finer than 0.25 microns. Semiconductor firms have urged the government to permit manufacturing of 0.18-micron chips. Wu noted that there had been a consensus at Taiwan's Sustainable Economic Development Conference in late-July that Taiwan's restrictions on information technology

investment should follow international standards set by the Wassenaar Arrangement. The Director commented that high-tech industry representatives had repeatedly raised this kind of issue with him during his November 29 trip to the Hsinchu Science Park (ref B), emphasizing the importance of government maintaining good relations with business.

Changes in 40 Percent Ceiling Under Consideration

18. (C) The Director mentioned the recent announcement by Carlyle Group, a U.S. investment firm, that it would purchase Advanced Semiconductor Engineering (ASE), a Taiwan semiconductor packaging and testing firm. The Director noted there has been substantial press speculation that the Carlyle-ASE deal is being driven by a desire for ASE to circumvent Taiwan's 40 percent ceiling on investment in China. (Note: Taiwan restricts the amount of capital its firms can invest in the PRC as a percentage of total capital. The restriction is usually called the 40 percent ceiling, but it is actually a sliding scale that limits larger firms to as little as 20 percent of total capital. End note.) Wu stressed that the Carlyle-ASE deal had nothing to do with the 40 percent ceiling, explaining that ASE had invested only 10 percent of its capital in the PRC. Wu accused some media outlets of falsely blaming the Carlyle-ASE deal on the 40 percent ceiling in order to make the government look bad while relaxation of the ceiling was being discussed in the Legislative Yuan. (Note: KMT legislator Lai Shyh-bao on December 4 proposed a bill to ease the investment cap. DPP and TSU legislators joined forces to defeat the measure and on November 29, TSU Legislative Whip David Huang suggested the cap should be tightened up rather than eased. End Note.)

19. (C) Wu commented that the TSU had "battered" the administration on the 40 percent ceiling during SEDC discussions. With rumors afloat that the TSU was considering supporting a no-confidence motion on

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President Chen, Wu explained, the administration had been unable to move forward on reviewing the 40 percent rule. However, he emphasized that the government is fully aware that this is a serious policy issue. Wu explained that MAC was examining the possibility of applying different ceilings to different industries. He said this was necessary because MAC's research indicates that 70 percent of the firms that have reached the 40 percent ceiling have financial problems. According to Wu, MAC will determine which industries have the most potential to earn a profit in the Mainland and raise the ceilings accordingly. This will shield the government from criticism that it approved investment for financially troubled firms. (Comment: We see logic in instituting different ceilings to limit investment in industries that the Taiwan authorities deem strategic. However, the idea that the authorities are better equipped than investors to determine where there are good business opportunities, does not seem to us to be a sound basis for policy. Wu's noting the status of negotiations with the TSU over investment applications in China is the most direct acknowledgement by a Chen Administration official that the TSU determines cross-Straits economic policy in Taiwan. End comment.)

But No Progress on Financial Sector

10. (C) On further opening of banking and other financial services, however, Wu acknowledged to the Director that there had not been much progress. He pointed out that on November 15 Beijing had released an announcement requiring that financial supervisory mechanisms be in

place before investment would be allowed by foreign banks. MAC had previously insisted that such bilateral mechanisms were necessary before Taiwan banks could invest in the Mainland. Wu pointed out that MAC believes negotiations are necessary to create these mechanisms. Therefore, he said, MAC and Financial Supervisory Commission officials had asked PRC counterparts about the possibility of such negotiations during a recent conference in Sichuan. The PRC officials, however, had replied that the PRC would negotiate only with parties that have accepted the "one China" principle, clearly signaling that it is not ready to negotiate on this issue yet.

MAC-TAO Exchanges

¶11. (C) On the other hand, Wu was pleased to report that MAC Legal Affairs Department Director Yang Jia-jiun had traveled to the PRC last week to discuss criminal investigation cooperation. While in the Mainland, he met with his counterpart at the Taiwan Affairs Office, which Wu described as a major breakthrough. (Comment: To our knowledge, this is the highest level MAC visit to the Mainland. End comment.) Wu also said that TAO will send a low-level group to Taiwan in January but did not provide details.

Su Resignation Likely if DPP Loses Kaohsiung

¶12. (C) When the Director asked about the future of the Su cabinet in the event of a DPP loss in the mayoral election in Kaohsiung, Wu commented that a tradition had developed of both the Premier and the DPP Chairman resigning after a major electoral loss. He said Su would probably resign as early as March in any event in order to launch his campaign for the presidency, since the DPP would determine its candidate in June or July. Wu believes that if the DPP loses Kaohsiung it will give Su a useful opportunity to resign and appear "principled." The entire cabinet would submit its resignation if the Premier resigns, Wu said, and it would be up to the next Premier to decide if Wu could continue as MAC Chairman.

Comment

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¶13. (C) While Joseph Wu is generally on the optimistic side of the spectrum in discussing cross-Strait progress, we believe there really is some quiet forward movement at work here. It strikes us that Beijing's facilitation of this progress can be read as paving the way to more dramatic advances with whomever emerges as Taiwan's next president. The simple fact is that the PRC dug itself into a hole by refusing to deal with the Chen administration from the get-go and is now anxious to move forward on something that is patently beneficial to both sides of the Strait.

YOUNG